

A REPORT TO INDIANA CITIZENS ON THE STATE'S FINANCES



*Connie K. Nass
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Dear Indiana Citizens:

Once again, it is my pleasure to present you with our semi-annual Report to Indiana Citizens on the State's Finances. December 31, 2003 marked the halfway point for Indiana government's 2004 fiscal year. This Report provides you with critical State fiscal data in an easy to understand format. Some of the conclusions one might draw from this information are as follows:

- For the third year in a row, we have a negative balance in the General Fund and Property Tax Replacement Fund Surplus at the mid-point of the State fiscal year, as shown on page 2. This is the "checking account" used to run day to day government operations. At first glance, the June and December 2003 Surpluses appear slightly higher than the prior year's. However, as we note in our commentary, when payment delays and annual cash transfers are taken into account, the State's balances are actually lower than they were one year ago.
- Over the past three and one-half fiscal years, we have seen State government's cash and investment balances fall by over 60%, leaving Indiana government with less and less money to cover shortfalls and placing the State's ultimate ability, and responsibility, to pay its bills in a precarious position.
- Over the past two fiscal years, the State has witnessed an increase in personal service expenditures (salaries, benefits, and some contracts) of nearly \$100 million, or over 5.5% (page 4). These increases accompanied a decrease in the number of full-time State employees and a State Retirement Incentive Program that was supposed to result in decreased costs to the State.
- The funding of Indiana government has become more dependent upon Riverboat Wagering Taxes. The "Big Three" – Sales Taxes, Individual Income Taxes, and Corporate Income Taxes – are now the "Big Four" with the addition of Riverboat Wagering Taxes as a major funding source for Indiana government's \$22.8 billion biennial budget.

Our government leaders need the input of a well-informed public to get Indiana government finances back on the right track. I hope this publication helps Hoosiers better understand the true state of Indiana government's finances. Please e-mail your questions or comments to comments@audlan.state.in.us, or call (317) 232-3300. This Report along with other valuable information is also available on our website at www.in.gov/auditor.

Sincerely,
Connie Nass
Auditor of State

Cash and Investment Balances (all funds) as of December 31, 2003

	Surplus Accounts	Non- Surplus Accounts	Total
General Fund Cash and Investments	\$(1,376,366,830)	\$ 881,810,132	\$ (494,556,697)
Rainy Day Fund	255,610,309		255,610,309
Total General Fund Cash and Investments	(1,120,756,520)	881,810,132	(238,946,388)
Non General Fund Cash and Investments		1,869,708,709	1,869,708,709
Property Tax Replacement Fund	509,827,774		509,827,774
Total Non General Fund Cash and Investments	509,827,774	1,869,708,709	2,379,536,483
Grand Total All Funds Cash and Investments	\$ (610,928,746)	\$2,751,518,841	\$2,140,590,095

General Fund and Property Tax Replacement Fund Surplus (“Surplus”)

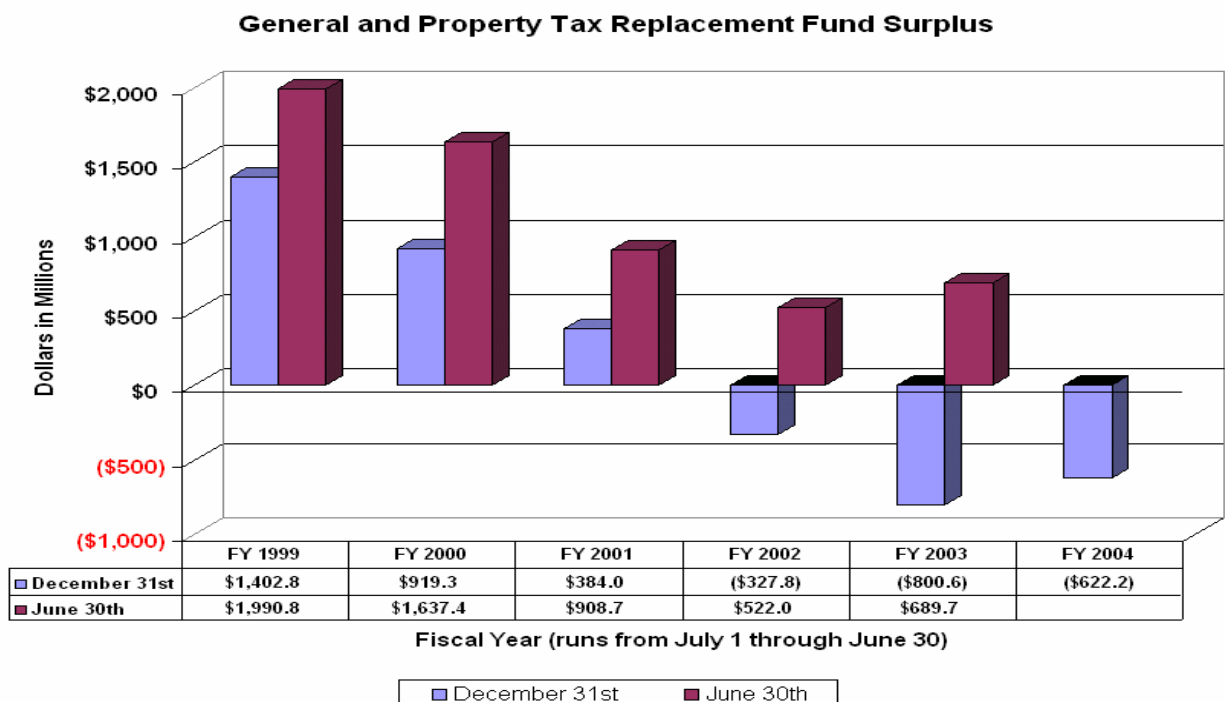
Indiana’s “General Fund and Property Tax Replacement Fund Surplus” (“Surplus”) is the State’s checking account, supporting the day to day operations of State government. The Surplus includes the Property Tax Replacement Fund, the Reserve for Tuition Support, the Rainy Day Fund, and the accounts that revert to the General Fund at the end of the fiscal year. By law the Surplus must be no less than zero on June 30.

The graph at the bottom of this page shows the Surplus on December 31, the mid-point of each fiscal year, and June 30, the end of each fiscal year, for December 1998 through December 2003. The Surplus has decreased from a high of \$1.991 billion on June 30, 1999 to a low of \$522.0 million on June 30, 2002. The Surplus increased slightly by June 30, 2003 to \$689.7 million. The December 31, 2003 Surplus is a negative \$622.2 million. **For the third year in a row the State has had a negative Surplus on December 31.**

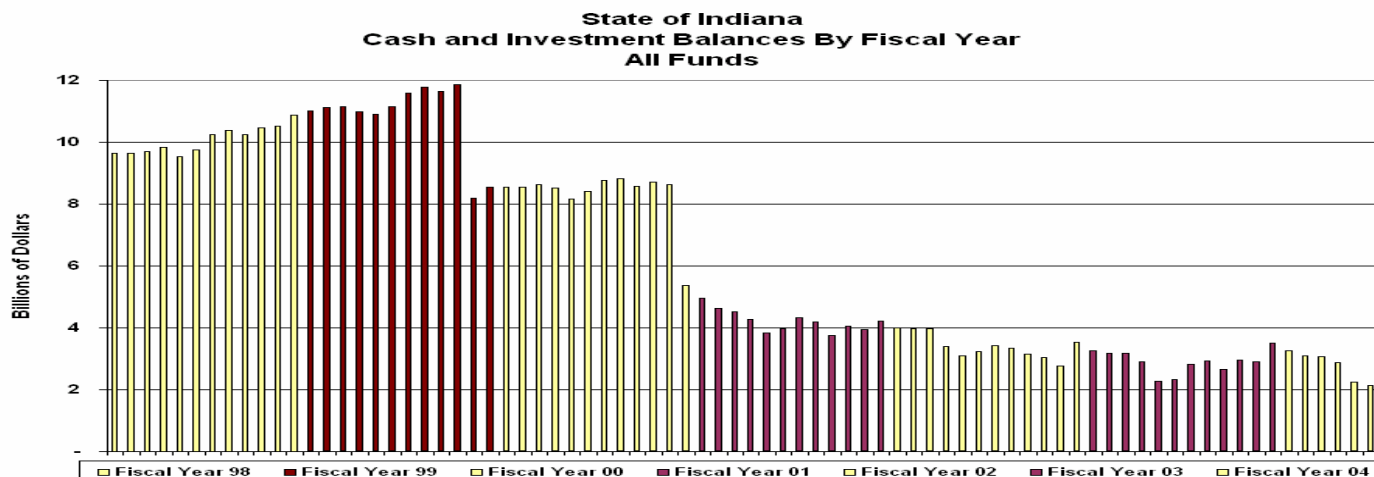
The December 31 deficits are caused in part by July cash transfers to certain non-reverting accounts and funds outside the General Fund. These transfers are made at the beginning of each fiscal year to cover the year’s anticipated expenses. The transfers, which are authorized by the biennial budget bill, cover items such as the State match for the Federal Medicaid program, and were \$850 million on December 31, 2002 and \$579 million on December 31, 2003. **Taking these transfers into account, the December 31, 2003, Surplus was actually \$93 million lower than the December 31, 2002, Surplus.**

The June 30, 2002 and 2003 Surplus balances are positive in part because of payment delays to schools for tuition support and to counties for the property tax replacement and homestead credits. The payment delays totaled \$373.7 million on June 30, 2002 and \$661.9 million on June 30, 2003. **As with the December 31 transfers, taking into account the payment delays, the June 30, 2003 Surplus is \$120.5 million less than the June 30, 2002 Surplus.**

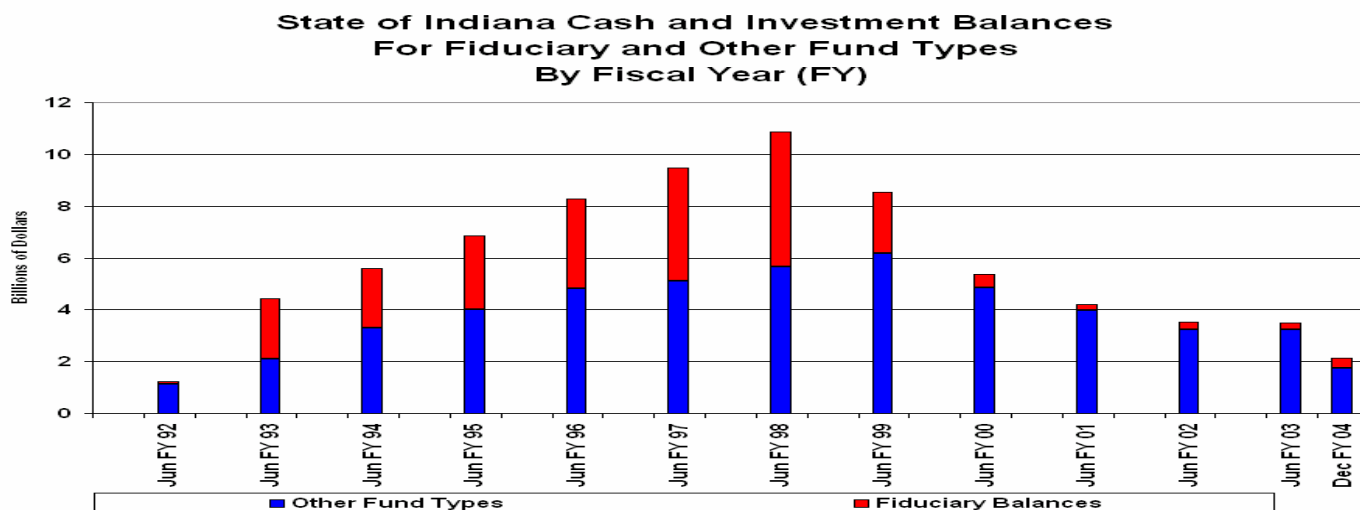
We therefore see the continuation of the downward trend in our state government's finances. The month to month Surplus remains negative throughout most of the fiscal year and the constitutional requirement of a balanced budget is still only met through significant payment delays to our schools and local governments.



Cash and Investment Balances (all funds)



The graph above shows the decline in the State's cash and investment balances for all funds from July 1997 (FY 98) through December 2003 (FY 04). The balance was \$9.65 billion in July 1997 (FY 98) and rose to a high of \$11.86 billion in April 1999 (FY 99). By December 31, 2003 (FY 04) the cash and investment balance had decreased to \$2.14 billion. The decrease of \$3.68 billion in May 1999 (FY 99) and \$3.26 billion in June 2000 (FY 00) resulted from the Teachers' Retirement Fund and the Public Employees' Retirement Fund becoming entities independent of State government.



This graph shows that not all cash and investments are available to fund the day to day operations of State government. Fiduciary funds (shown in red), which the State holds in trust for the benefit of others, by law are restricted and may not be used for the State government's general operations. The graph shows fiscal year end (June 30) cash and investment balances for FY 92 through FY 03 as well as the December 31, 2003 (FY 04) balance. Only the cash and investments represented by the blue portion of the graph could be made available to cover negative cash balances in the General Fund and Property Tax Replacement Fund.

The total cash and investment balances have declined by 60.14%, from \$5.37 billion on June 30, 2000 down to \$2.14 billion on December 31, 2003. The non-fiduciary fund balances reached a high of \$5.65 billion on Jun 30, 1998 and are down to a low of \$1.75 billion as of December 31, 2003. If this trend continues, the state's ability to pay its day to day obligations will be compromised.

State Employment Data

Full Time State Employees Paid Through The Auditor of State's Office December 1999 - December 2003

Agency or Function of Government	Dec, 1999	Dec, 2000	Dec, 2001	Dec, 2002	Dec, 2003
Conservation, Culture and Development	3,731	3,758	3,722	3,678	3,646
Department of Corrections	7,186	7,723	7,915	8,238	8,311
Dept of Transportation	4,330	4,302	4,282	4,249	4,129
Family and Social Services Agency (FSSA)	10,409	10,466	10,304	9,980	9,789
General Government	2,463	2,472	2,466	2,320	2,351
Health	2,098	2,108	2,053	2,042	2,107
Motor Vehicle Commission	1,516	1,548	1,524	1,574	1,607
Public Safety	1,849	1,907	1,896	1,874	1,910
State Police	2,020	2,000	1,972	1,952	1,903
Total Governor's Authority	35,602	36,284	36,134	35,907	35,753
Employees on Disability Leave	1,159	1,235	1,263	1,315	1,217
Judiciary	816	836	862	869	899
Other Elected Officials	1,016	1,014	1,018	1,021	1,039
Grand Total	38,593	39,369	39,277	39,112	38,908
Salaries	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Benefits	\$1,139,187,253	\$1,193,955,033	\$1,272,381,257	\$1,279,342,544	\$1,289,672,794
Subtotal	373,734,662	411,990,467	452,750,147	498,924,031	521,498,289
Contract Employees *	1,512,923,914	1,605,947,500	1,725,133,405	1,778,268,577	1,811,173,087
Total Personal Services	47,770,065	69,174,643	69,790,197	74,999,467	82,815,794
	\$1,560,691,980	\$1,675,120,143	\$1,794,921,602	\$1,853,266,042	\$1,893,986,878
Benefits as a % of Salaries	32.81%	34.51%	35.58%	39.00%	40.44%

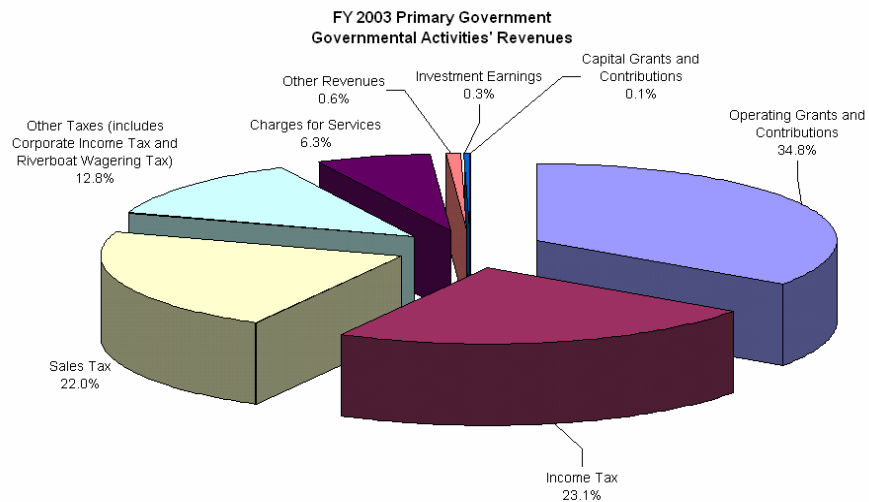
* amounts do not include all temporary or contract workers

State Retirement Incentive Program (SRIP) Analysis December 2001 - December 2003

Agency or Function of Government	Dec, 2001	Adds	Left	Left for SRIP	Dec, 2002	Adds	Left	Left for SRIP	Dec, 2003	SRIP Rehired By Contract	SRIP Rehired As Employee
Governor's Authority	36,134	4,518	4,701	44	35,907	4,724	3,691	1,187	35,753	14	2
Employees on Disability Leave	1,263	612	554	6	1,315	510	522	86	1,217	-	-
Judiciary	862	52	44	1	869	141	107	4	899	-	-
Other Elected Officials	1,018	147	143	1	1,021	152	121	13	1,039	3	-
Grand Total	39,277	5,329	5,442	52	39,112	5,527	4,441	1,290	38,908	17	2

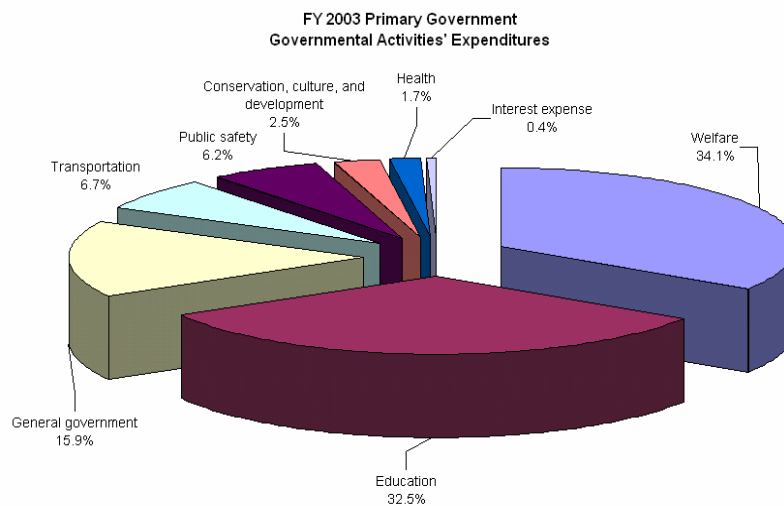
Revenues and Expenditures of the Primary Government FY 2003 (GAAP Basis of Accounting)

Where the money comes from:



Taxes account for almost 60% of Indiana's revenues, of which 75% comes from individual income tax and sales tax. The State sales tax increased 20%, from 5% to 6%, effective December 1, 2002. Operating grants represent more than one-third of Indiana's revenues, the biggest component of which is Federal grants received for specific purposes.

Where the money is spent:



The largest portion of the State's expenses (34.1%) is Welfare, which includes \$4.1 billion spent for Medicaid assistance. Approximately 2/3 of this expense is funded through operating grants (largely federal), with the remainder funded by general revenues. Education, which makes up 55.7% of the General Fund budget, comprises 32.5%, or \$6.2 billion, of the State's total expenses and is funded mostly from general revenues. Education expenses are composed of tuition support, transportation, and the ADA (average daily attendance) flat grant distribution.

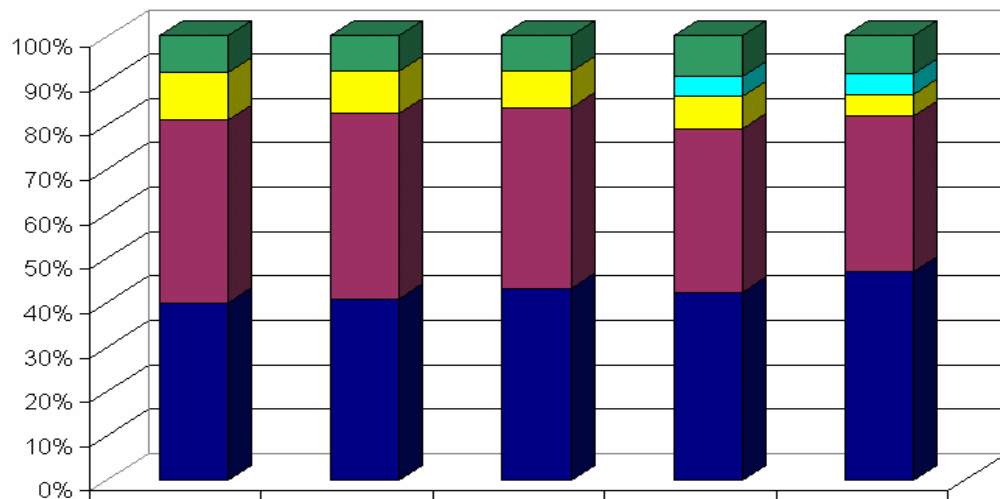
General and Property Tax Replacement Fund Revenue Trends (Cash Basis)

A Detailed Analysis of the Four Primary Revenue Sources

The General Fund and Property Tax Replacement Fund receive revenue from sales tax, individual income tax, corporate income tax, riverboat wagering tax, and 8% from various other revenue sources. During fiscal year 2003, the revenue mix was changed by the General Assembly, increasing the sales tax percentage and authorizing the deposit of riverboat wagering tax into the funds. In fiscal years 2000 through 2002, sales, individual, and corporate taxes remained stable, accounting for approximately 92% of the revenues. By December 31, 2003 that percentage had decreased to 86.9%. **Riverboat taxes are now a major component of the State's \$22.8 billion biennial budget.**

General and Property Tax Replacement Fund Revenue Percentage by Type

The State's budget is prepared based on revenue forecasts. Therefore, deficits are greater when actual revenues fall below the forecast amount.

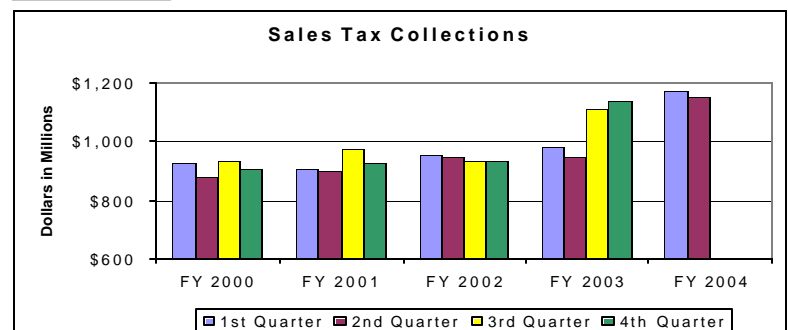


Other Revenue	8.2%	8.0%	8.0%	9.1%	8.5%
Riverboat Wagering Tax				4.4%	4.6%
Corporate Income Tax	10.8%	9.4%	8.1%	7.4%	4.8%
Individual Income Tax	41.1%	41.8%	40.7%	36.9%	35.2%
Sales Tax	39.9%	40.8%	43.2%	42.2%	46.8%

Sales Tax

In the first half of fiscal year 2004, sales taxes accounted for 46.8% of the General Fund and Property Tax Replacement Fund revenue (General Fund revenue). For the first half of FY 04, sales tax receipts were \$400.4 million (20.8%) higher than the previous year. **The increase is largely due to the 20% increase in the tax rate from 5% to 6% that became effective December 1, 2002. However, receipts were still \$91.5 million (3.8%) below the target that was set April 10, 2003 by the Economic Forecast Committee.**

Sales Tax (Dollars in Millions)					
	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004
1st Quarter	928.1	903.9	953.1	978.9	1,172.8
2nd Quarter	877.1	895.3	942.3	945.6	1,152.0
3rd Quarter	936.9	970.1	933.3	1,111.7	-
4th Quarter	909.3	924.6	932.7	1,136.4	-
Total	3,651.4	3,693.9	3,761.4	4,172.6	2,324.8



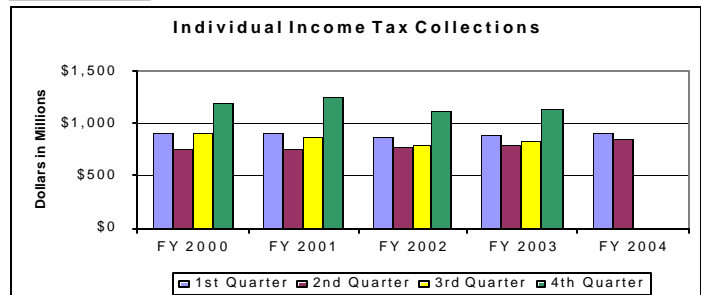
General and Property Tax Replacement Fund Revenue Trends (Cash Basis)

A Detailed Analysis of the Four Primary Revenue Sources (Continued)

Individual Income Tax

Individual income taxes accounted for 35.2% of General Fund revenue in the first half of FY 04. First half FY 04 revenue was \$61.2 million (3.6%) above the amount collected for the same period in FY 03 but was \$25.9 million (1.5%) below the revenue target prepared April 10, 2003 by the Economic Forecast Committee. **Individual income tax revenue, which had been decreasing monthly on a year to year basis, began an upward trend starting in August of 2002.** In the previous 25 months, July 2000 through July 2002, the 12 month average revenue had declined by an average of three tenths of a percent per month. Since August 2002 the 12 month average revenue has averaged a three tenths of a percent increase per month with a decline in only five of those 17 months.

Individual Income Tax (Dollars in Millions)					
	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004
1st Quarter	901.5	912.6	860.2	884.7	904.0
2nd Quarter	745.5	762.1	770.8	799.7	841.6
3rd Quarter	906.5	859.3	793.7	832.8	-
4th Quarter	1,199.8	1,245.8	1,116.1	1,127.1	-
Total	3,753.3	3,779.8	3,540.8	3,644.3	1,745.6

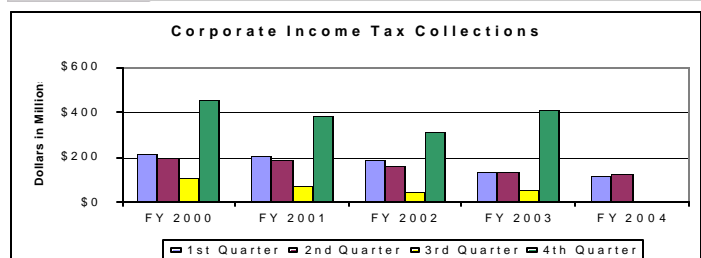


Corporate Income Tax

Corporate income tax revenue continues to decline and for the first six months of FY 04 accounted for only 4.8% of the General Fund revenue compared to 10.8% in FY 00.

During the first six months of FY 04, each month's revenue has been lower than the same month in the previous year. The first six months' revenue of \$240.0 million was \$32.8 million (12.0%) below the \$272.8 million revenue for the first six months of FY 03, and \$114.3 million (32.3%) below the \$354.3 million revenue for the first six months of FY 02. The revenue for the first six months of FY 04 was \$12 million (4.8%) below the \$252 million revenue target prepared by the Economic Forecast Committee on April 10, 2003. **The change in the twelve month moving average of corporate income tax revenue has been positive only 13 times in the 42 months that began July, 2001.**

Corporate Income Tax (Dollars in Millions)					
	FY 2000	FY 2001	FY 2002	FY 2003	FY 2004
1st Quarter	220.4	205.6	189.8	132.3	114.2
2nd Quarter	199.7	187.9	164.5	140.5	125.8
3rd Quarter	108.6	75.7	44.2	50.2	-
4th Quarter	456.6	386.1	310.9	406.1	-
Total	985.3	855.3	709.4	729.1	240.0



Riverboat Wagering Tax

Riverboat wagering tax accounted for 4.6 % of the General Fund revenue in the first half of FY 04 compared to none in FY 00.

Prior to FY 03 the State's share of the riverboat wagering tax was deposited into the Build Indiana Fund. Starting with FY 03 the State's share of the riverboat wagering tax is deposited into the Property Tax Replacement Fund. At the end of each fiscal year beginning with FY 03, funds are to be transferred to the Build Indiana Fund to bring its revenue total to \$250 million. In FY 03, \$136,209,071 was transferred. The State's share of riverboat wagering tax for fiscal years 2000 - 2004 was as follows:

FY 2000 \$246,114,118
FY 2001 \$260,193,774
FY 2002 \$285,139,922
FY 2003 \$430,886,629
FY 2004 (first half) \$228,637,277

Riverboat Wagering Tax (Dollars in Millions)			
	FY 2003		FY 2004
1st Quarter	Prior to fiscal year 2003 riverboat wagering taxes were not deposited into the General and Property Tax Replacement Funds.		49.4
2nd Quarter			86.2
3rd Quarter			118.3
4th Quarter			176.9
Total			430.8

